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IN THE

Supreme Court of the United States

VISION SERVICE PLAN,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF OF AMICUS CURIAE DARRYLL K. JONES IN SUPPORT OF PETITIONER

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INTEREST OF AMICUS CURIAE

Amicus Curiae Darryll K. Jones is a Professor of Law at Stetson University College of Law in Gulfport, Florida.[1] He has served in that position for two years. Prior to that, Professor Jones served as Assistant and Associate Professor of Law and Associate Dean of Academic Affairs at the University of Pittsburgh, Pittsburgh, Pennsylvania. He served in those positions, sequentially from September 1999 until August 2006. He presently serves as co-editor of the Nonprofit Law Professor Blog, accessible online at *http://lawprofessors.typepad.com/nonprofit/*. Prior to entering the teaching profession, Professor Jones served as Associate General Counsel at the University of Florida, specializing in tax exempt law, and as General Counsel at Columbia College Chicago.

Professor Jones has written and practiced extensively in the area of tax exempt organizations. His publications include *The Tax Law of Charities and Other Exempt Organizations* (2d ed. 2007), *Third Party Profit-Taking In Tax Exemption Jurisprudence*, 2007 Brigham Young University Law Review 977 (2007), *The Scintilla of Individual Profit: In Search of Private Inurement and Excess Benefit*, 19 Virginia Tax Review

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1. No party or counsel for any party authored any portion of this brief or made a monetary contribution intended to fund the preparation or submission of the brief. No entity other than amicus curiae Darryll K. Jones or his counsel monetarily contributed to the preparation or submission of this brief. The Petitioner and the Respondent were given timely notice of the intent to file this brief under Supreme Court Rule 37, and both parties consented to the filing of this brief.

575 (2000), and *Tax Exemption Issues Facing Academic Health Centers in the Managed Care Environment*, 24 Journal of College and University Law 261 (1997) among several other publications regarding tax exemption. His publication, *When Charity Aids Tax Shelters*, 4 FLORIDA TAX REVIEW 769 (2001), served as a model for a provision subsequently enacted by Congress in an effort to police the involvement of tax exempt organizations in improper tax shelter transactions. *See* I.R.C. § 4965. Professor Jones's particular interest with respect to this case involves the application of the "private benefit" doctrine, under which the Internal Revenue Service ("the Service") denies or revokes tax exempt status on the basis that an organization improperly benefits private, noncharitable individuals.

SUMMARY OF ARGUMENT

This case involves a matter of extreme importance to the entire nonprofit health maintenance organization (HMO) industry. The court below held, based upon an unexplained and misunderstood application of the private benefit doctrine, that an HMO operating under a membership structure primarily served the private benefit of its subscribers and, therefore, is not entitled to tax exemption under section 501(c)(4) of the Internal Revenue Code. It is true that the private benefit doctrine is implicated when a nonprofit organization confers private benefit on non-charitable recipients, such as the members of the HMO. The private benefit doctrine, however, does not preclude an organization from economic dealings with a non-charitable class of persons when doing so is *necessary* to accomplish its charitable or social-welfare purpose. For example,

nonprofit hospitals routinely provide "profits" in the form of compensation to physicians and other service providers that they employ to achieve their charitable healthcare goals. Likewise, nonprofit HMOs cannot possibly achieve their charitable purpose without a membership form of organization.

The fatal flaw in the Ninth Circuit's analysis and conclusion is that (1) it fails to heed to Congress's explicit statement to the contrary and (2) it adopts a rule entirely without regard to the context surrounding the health care market place. As to the first flaw, Congress has explicitly stated that nonprofit HMOs shall not be excluded from tax exemption. *See* I.R.C. § 501(m)(3). By contrast, the court below ruled that a membership form of organization, even one providing for a subsidized dues program, precludes tax exemption. This holding directly contradicts clear congressional intent. Congress specifically exempted "health maintenance organizations" from the definition of commercial insurance activities. *See* I.R.C. § 501(m)(3)(B). In so doing, Congress was describing organizations whose defining characteristic is their existence as associations formed to control healthcare costs, to increase the supply of health care services, and to extend those services to individual unable to pay for their own care.

As to the second flaw, the modern health care marketplace demands that health care providers deliver large and predictable patient volume that can only be derived from a membership base. Virtually all HMOs are "organizations" of members who band together to obtain health services from nonprofit providers. A judicially imposed rule precluding tax exemption for

HMOs because of their invariable "membership" structure would effectively preclude tax exemption for all nonprofit HMOs, making a dead letter of Congress's careful effort to preserve tax exemption for such "organizations" of subscribers. HMOs without members have never existed and, in any event, could not compete with for-profit HMOs in order to achieve their charitable purpose of providing indispensable services.

The opinion below effectively raises a categorical bar against tax exemption for HMOs, the fiduciaries of whom seek the pubic good rather than private gain. Even as they pursue the public good, nonprofit HMO's must engage for-profit service providers. Like all tax-exempt entities, nonprofit HMOs must enter into contracts and compete for goods and services also sought by the for-profit sector. The fiduciaries of nonprofit HMO's are not exempt from the market forces prevalent in society merely because they eschew private profit in support of the public good. Thus, nonprofit HMOs, just like any other nonprofit entity must necessarily comply with implicit market rules to achieve their charitable purpose. A rule prohibiting HMOs from adopting the organizational membership structure, a structure absolutely demanded in the marketplace, effectively denies tax exempt status to all nonprofit HMOs.

ARGUMENT

A. The Membership Organization Proscribed by the Court Below Is Necessary to the Accomplishment of the Charitable and Social-Welfare Purpose for Which Congress Has Granted Tax Exemption.

The court below essentially held that a membership form of organization results in private benefit to the members and, thus, precludes tax exemption. The conclusion represents a fundamental misunderstanding of the factors necessary to achieve a charitable or social welfare purpose. The conclusion fails to distinguish effect from intent. As noted by the Internal Revenue Service and at least two commentators, private benefit is an inevitable prerequisite to the accomplishment of a charitable or social welfare purpose. Darryll K. Jones, *Third Party Profit-Taking In Tax Exemption Jurisprudence*, 2007 BYU L. Rev. 977, 981 (2007); John D. Columbo, *In Search of Private Benefit*, 58 Fla. L. Rev. 1063 (2006). In short, the public good cannot be achieved without private benefit. This is especially true with regard to a public good that is at once indispensable to the social good and subject to monopolization by for-profit healthcare providers.

Charitable health care and health care services provided for the purpose of increasing social welfare cannot possibly be accomplished without the cooperation of for-profit service providers, such as physicians who either provide the actual services or insurers who actually subsidize charitable health care via payments to nonprofit health care providers. That cooperation is gained exclusively through the ability of nonprofit health

care organizations to offer economic incentives comparable to those available from for-profit health care providers. As noted above, for-profit HMOs utilize a membership base to deliver larger patient volume to practitioners and negotiate lower fees payable by insurers. Through this process, investors in the for-profit HMOs achieve a return on their investment. Nonprofit health care organizations rely upon the same service providers and third party payers to extend those vital health care services to the poor and to encourage the search for new cures. Thus, nonprofit health care organizations must necessarily offer incentives similar to those available from for-profit health care organizations. Doing so is not indicative of intent to enrich private individuals but rather is necessary to harness market resources for the public good in a manner suitable for tax exemption.

B. Precluding Tax Exemption Because of an HMO's Membership Structure Effectively Repeals Tax Exemption Granted by Congress and Prevents All HMOs from Operating Charitably.

For the reasons explained above, a judicially imposed rule precluding tax exemption for HMOs because of their invariable membership structure would effectively preclude tax exemption where Congress has explicitly granted tax exemption. As a doctrinal matter, this outcome is directly contrary to Congress's intent. Petitioner's Petition for Writ of Certiorari adequately states the proposition:

> In 1986, Congress reviewed the tax-exempt status of health care companies in light of

> changes in the health care marketplace, particularly the increase in competitive, for-profit health insurers. As part of the Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2085, Congress adopted what is now Code section 501(m). This section denies a tax exemption under 501(c)(3) and 501(c)(4) to organizations that offer "commercial-type insurance."
>
> At the same time that it revoked tax exemptions for providers of "commercial-type insurance," however, Congress expressly retained the existing tax-exempt status for nonprofit HMOs, including HMOs offering supplemental services such as vision or dental plans. Section 501(m)(3)(B) thus provides that "commercial-type insurances should *not* include "incidental health insurance provided by a health maintenance organization of a kind customarily provided by such organizations."

(Pet. for Cert. at 15-16 (footnote omitted).) Petitioner's brief continues by correctly explaining that Congress later confirmed that it intended to allow the availability of tax exempt status for organizations that "'operate in the same manner as a health maintenance organization'" (*id.* at 16). As noted above, the membership form of organization is the single defining characteristic of HMOs. Thus, the conclusion is inescapable that Congress explicitly intended to make tax exemption available to organizations that have members in an effort to increase the amount of health care services in the marketplace without limiting those services solely to those who are able to afford such services.

By contrast, the court below relied exclusively on the very characteristic defining HMOs as the basis for precluding those organizations from tax exempt status. Should its analysis prevail, the court below will have effectively overruled Congress's judgment that a membership organization is no bar to tax exempt status. Indeed, as explained above and as recognized by the market itself, utilizing a membership structure is essential to offering healthcare services whether on a for-profit or a nonprofit tax-exempt basis.

CONCLUSION

Petitioner and other amici curiae have convincingly set forth the legal basis that compels review of the opinion of the court below. The broader purpose of this brief is to place the opinion of the court below in the context of the for-profit and nonprofit health care marketplace. The opinion of the court below fails to consider the real-world healthcare marketplace in which its conclusion is to apply. Instead, it adopts an arbitrary rule without regard to the historical context in which nonprofit HMOs have existed and reaches a conclusion that, if sustained, will categorically preclude tax exemption for all nonprofit HMOs; the defining quality – indeed the factor absolutely necessary to the existence of nonprofit HMOs – is the membership structure found disqualifying by the court below. This is most certainly contrary to Congressional intent and, even worse, decreases the amount of charitable health care available to society. For these reasons, the Petition for Certiorari should be granted.

Respectfully submitted,

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